

## Internal Revenue Service, Treasury

## § 1.565-1

(b) *Dividend carryover from year in which taxpayer was not a personal holding company.* In computing the dividend carryover, the taxable income as adjusted under section 545 of any preceding taxable year shall be determined as if the corporation was, under the law applicable to such taxable year, a personal holding company.

(c) *Dividend carryover from year in which taxpayer was subject to 1939 Code.* In a case where the first or the second preceding taxable year began before the taxpayer's first taxable year under the Internal Revenue Code of 1954, the amount of the dividend carryover shall be determined under the Internal Revenue Code of 1939.

(d) *Statement to be filed with return.* Every corporation claiming a dividend carryover for any taxable year shall file with its return for such year a concise statement setting forth the amount of the dividend carryover claimed and all material and pertinent facts relative thereto, including a detailed schedule showing the computation of the dividend carryover claimed.

(e) *Computation of dividend carryover.* The computation of the dividend carryover may be illustrated by the following examples:

*Example 1.* The X Corporation, which files its income tax returns on the calendar year basis, has taxable income, adjusted as required by section 545, in the amount of \$110,000 and has a dividends paid deduction of \$150,000 for the year 1954. For 1955, its taxable income, adjusted as required by section 545, is \$200,000 and its dividends paid deduction is \$300,000. The dividend carryover to the year 1956 is \$140,000, computed as follows:

Dividends paid deduction for 1954 .....	\$150,000
Taxable income for 1954 .....	110,000
Dividend carryover from 1954 .....	40,000
Dividends paid deduction for 1955 .....	300,000
Taxable income for 1955 .....	200,000
Dividend carryover from 1955 .....	100,000
Dividend carryover for 2 preceding taxable years, allowable as a deduction for the year 1956 .....	140,000

*Example 2.* The Y Corporation, which files its income tax returns on the calendar year basis, has taxable income, adjusted as required by section 545, in the amount of \$100,000 and has a dividends paid deduction of \$150,000 for the year 1954. For 1955, its taxable income, adjusted as required by section 545, is \$200,000 and its dividends paid deduction is

\$170,000. The dividend carryover to the year 1956 is \$20,000 computed as follows:

Dividends paid deduction for 1954 .....	\$150,000
Taxable income for 1954 .....	100,000
Dividend carryover from 1954 .....	50,000
Taxable income for 1955 .....	200,000
Dividends paid deduction for 1955 .....	170,000
Excess of taxable income over dividends paid deduction .....	30,000
Dividend carryover for second preceding taxable year, allowable as a deduction for the year 1956 .....	20,000

### § 1.565-1 General rule.

(a) *Consent dividends.* The dividends paid deduction, as defined in section 561, includes the consent dividends for the taxable year. A consent dividend is a hypothetical distribution (as distinguished from an actual distribution) made by:

(1) A corporation that has a reasonable basis to believe that it is subject to the accumulated earnings tax imposed in part I of subchapter G, chapter 1 of the Code, or

(2) A corporation described in part II (personal holding companies or a corporation with adjusted income from rents described in section 543(a)(2)(A) which utilizes the consent dividends described in section 543(a)(2)(B)(iii) to avoid personal holding company status) or part III (foreign personal holding companies) of subchapter G or in part I (regulated investment companies) or part II (real estate investment trusts) of subchapter M, chapter 1 of the Code.

A consent dividend may be made by a corporation described in this paragraph to any person who owns consent stock on the last day of the taxable year of such corporation and who agrees to treat the hypothetical distribution as an actual dividend, subject to the limitations in section 565, § 1.565-2, and paragraph (c)(2) of this section, by filing a consent at the time and in the manner specified in paragraph (b) of this section.

(b) *Making and filing of consents.* (1) A consent shall be made on Form 972 in accordance with this section and the instructions on the form issued therewith. It may be made only by or on behalf of a person who was the actual

owner on the last day of the corporation's taxable year of any class of consent stock, that is, the person who would have been required to include in gross income any dividends on such stock actually distributed on the last day of such year. Form 972 shall contain or be verified by a written declaration that it is made under the penalties of perjury. In the consent such person must agree to include in gross income for his taxable year in which or with which the taxable year of the corporation ends a specific amount as a taxable dividend.

(2) See paragraph (c) of this section and § 1.565-2 for the rules as to when all or a portion of the amount so specified will be disregarded for tax purposes.

(3) A consent may be filed at any time not later than the due date of the corporation's income tax return for the taxable year for which the dividends paid deduction is claimed. With such return, and not later than the due date thereof, the corporation must file Forms 972 duly executed by each consenting shareholder, and a return on Form 973 showing by classes the stock outstanding on the first and last days of the taxable year, the dividend rights of such stock, distributions made during the taxable year to shareholders, and giving all the other information required by the form. Form 973 shall contain or be verified by a written declaration that is made under the penalties of perjury.

(c) *Taxability of amounts specified in consents.* (1) The filing of a consent is irrevocable, and except as otherwise provided in section 565(b), § 1.565-2, and paragraph (c)(2) of this section, the full amount specified in a consent filed by a shareholder of a corporation described in paragraph (a) of this section shall be included in the gross income of the shareholder as a taxable dividend. Where the shareholder is taxable on a dividend only if received from sources within the United States, the amount specified in the consent of the shareholder shall be treated as a dividend from sources within the United States in the same manner as if the dividend has been paid in money to the shareholder on the last day of the corporation's taxable year. See paragraph (b) of this section relating to the making

and filing of consents, and section 565(e) and § 1.565-5, with respect to the payment requirement in the case of nonresident aliens and foreign corporations.

(2) To the extent that the Commissioner determines that the corporation making a consent dividend is not a corporation described in paragraph (a) of this section, the amount specified in the consent is not a consent dividend and the amount specified in the consent will not be included in the gross income of the shareholder. In addition, where a corporation is described in paragraph (a)(1) but not paragraph (a)(2) of this section, to the extent that the Commissioner determines that the amount specified in a consent is larger than the amount of earnings subject to the accumulated earnings tax imposed by part I of subchapter G, such excess is not a consent dividend under paragraph (a) of this section and will not be included in the gross income of the shareholder.

(3) Except as provided in section 565(b), § 1.565-2 and paragraph (c)(2) of this section, once a shareholder's consent is filed, the full amount specified in such consent must be included in the shareholder's gross income as a taxable dividend, and the ground upon which a deduction for consent dividends is denied the corporation does not affect the taxability of a shareholder whose consent has been filed for the amount specified in the consent. For example, although described in part I, II, or III of subchapter G, or part I or II of subchapter M, chapter 1 of the Code, the corporation's taxable income (as adjusted under section 535(b), 545(b), 556(b), 852(b)(2), or 857(b)(2), as appropriate) may be less than the total of the consent dividends.

(4) A shareholder who is a nonresident alien or a foreign corporation is taxable on the full amount of the consent dividend that otherwise qualifies under this section even though that payment has not been made as required by section 565(e) and § 1.565-5.

(5) Income of a foreign corporation is not subject to the tax on accumulated earnings under part I of subchapter G, chapter 1 of the Code except to the extent of U.S. source income, adjusted as

permitted under section 535. See section 535 (b) and (d) and §1.535-1(b). Therefore, foreign source earnings (other than those distributions subject to resourcing under section 535(d)) of a foreign corporation that is not described in paragraph (a)(2) of this section cannot qualify for consent dividend treatment. Accordingly, a consent dividend made by a foreign corporation described in paragraph (a)(1) of this section shall not be effective with respect to all of the corporation's earnings, but shall relate solely to earnings which would have been, in the absence of the consent dividend, subject to the accumulated earnings tax.

[T.D. 8244, 54 FR 10538, Mar. 14, 1989]

#### § 1.565-2 Limitations.

(a) *General rule.* Amounts specified in consents filed by shareholders or other beneficial owners of a corporation described in §1.565-1(a) are not treated as consent dividends to the extent that—

(1) They would constitute a preferential dividend or

(2) They would not constitute a dividend (as defined in section 316),

if distributed in money to shareholders on the last day of the taxable year of the corporation. If any portion of any amount specified in a consent filed by a shareholder of a corporation described in the preceding sentence is not treated as a consent dividend under section 565(b) and this section, it is disregarded for all tax purposes. For example, it is not taxable to the consenting shareholder, and paragraph (c) of §1.565-1 is not applicable to this portion of the amount specified in the consent.

(b) *Preferential Distribution.* (1) A preferential distribution is an actual distribution, or a consent distribution, or a combination of the two, which involves a preference to one or more shares of stock as compared with other shares of the same class or to one class of stock as compared with any other class of stock. See section 562(c) and §1.562-2.

(2) The application of section 565 (b) (1) and §1.565-2 (b) may be illustrated by the following examples:

*Example 1.* The X Corporation, a personal holding company, which makes its income

tax returns on the calendar year basis, has 200 shares of stock outstanding, owned by A and B in equal amounts. On December 15, 1987, the corporation distributes \$600 to B and \$100 to A. As a part of the same distribution, A executes a consent to include \$500 in his gross income as a taxable dividend although such amount is not distributed to him. The X Corporation, assuming the other requirements of section 565 have been complied with, is entitled to a consent dividends deduction of \$500. Although the consent dividend is deemed to have been paid on December 31, 1987, the last day of the taxable year of the corporation, the total amount of all distributions constitutes a single nonpreferential distribution of \$1200.

*Example 2.* The Y corporation, a personal holding company, which makes its income tax returns on the calendar year basis, has one class of consent stock outstanding, owned in equal amounts by A, B, and C. If A and B each receive a distribution in cash of \$5,000 and C consents to include \$3,000 in gross income as a taxable dividend, the combined actual and consent distribution of \$13,000 is preferential. See section 562 (c) and §1.562-2 (a). Similarly, if no one receives a distribution in cash, but A and B each consents to include \$5,000 as a taxable dividend in gross income and C agrees to include only \$3,000, the entire consent distribution is preferential.

*Example 3.* The Z Corporation, which makes its income tax returns on the calendar year basis and is subject, for the taxable year in question, to the accumulated earnings tax, has only two classes of stock outstanding, each class being consent stock and consisting of 500 shares. Class A, with a par value of \$40 per share, is entitled to two-thirds of any distribution of earnings and profits. Class B, with a par value of \$20 per share, is entitled to one-third of any distribution of earnings and profits. On December 15, 1987, there is distributed on the class B stock \$2 per share, or \$1,000, and shareholders of the class A stock consent to include in gross income amounts equal to \$2 per share, or \$1,000. The entire distribution of \$2,000 is preferential, inasmuch as the class B stock has received more than its pro rata share of the combined amounts of the actual distributions and the consent distributions.

(c) *Section 316 Limitation.* (1) An additional limitation under section 565 (b) is that the amounts specified in consents which may be treated as consent dividends cannot exceed the amounts which would constitute a dividend (as defined in section 316) if the corporation had distributed the total specified amounts in money to shareholders on the last day of the taxable year of the